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No. 82-1905

In the Supreme Court of the United States

OCTOBER TERM, 1983

SUN CHEMICAL CORPORATION, ETC., PETITIONER

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FEDERAL CIRCUIT

MEMORANDUM FOR THE UNITED STATES IN OPPOSITION

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Petitioner contends that the court below erred in dismissing its suit for a refund of federal income taxes paid for 1960 and 1961 and on the grounds that: (1) the 1960 claim was barred by petitioner's failure to file a sufficient administrative claim for refund; and (2) the 1961 claim was barred by res judicata.

1. In November 1962, petitioner entered into a contract with the United States Air Force to design and make prototypes of a geodetic and photo mapping system and a ground data processing subsystem (Pet. App. A2, A34).[1] The contract was for the fixed sum of $6,718,480, but it was subject to a "change" clause authorizing the contracting officer to

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[1]The contract was actually entered into by Kollsman Instrument Corporation. Under a later merger, petitioner became Kollsman's successor in interest. For convenience, we will use the term "petitioner" to refer to Kollsman as well.

make changes subject to an equitable price adjustment for any cost differentials caused by the work changes (*id.* at A2, A35-A36). The Air Force made numerous changes and, on December 30, 1964, petitioner submitted its request for an equitable price increase of $5,528,205 (*id.* at A3, A38). In 1966, the Air Force contracting officer determined that petitioner was entitled only to an additional $123,780 (*id.* at A39). Petitioner appealed to the Armed Services Board of Contract Appeals, and, in September 1967, the parties agreed to an increase of $2,000,000 (*ibid.*).

Petitioner chose to compute its income under the "percentage of completion" method for long-term contracts then authorized by Treasury Regulations.[2] For 1963 through 1965, it reported anticipated gross income of $10,142,787 from the contract, which included its anticipated allowance for cost increases (Pet. App. A3, A40-A41). When the Air Force contracting officer initially limited the cost escalation to $123,780 in 1966, petitioner recomputed its income from the contract and determined that it had in fact suffered a loss of $4,359,000, which it then deducted on its 1966 tax return (*id.* at A3, A41-A42). When the $2,000,000 settlement was finally agreed to in 1967, petitioner recomputed its loss on the contract as $3,318,000 and deducted that amount on its 1967 federal income tax return in lieu of the $4,359,000 loss claimed on its 1966 return (*id.* at A3, A43).

On April 13, 1967, petitioner filed a claim for refund for the taxable year 1960, based on an asserted net operating loss carryback from 1963 (Pet. App. A3). This asserted loss

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[2]Under the percentage of completion method, the portion of the gross contract price that corresponds to the percentage of the entire contract completed during the taxable year must be included in gross income for such taxable year. All costs incurred during the taxable year with respect to the long term contract are deducted from this sum in arriving at taxable income. Treasury Regulations on Income Tax (1954 Code), Section 1.451-3(c) (26 C.F.R.).

carryback was based on an alternative method of reflecting petitioner's loss on the Air Force contract. Petitioner recomputed its 1963 income excluding, pro rata, the amounts that were in excess of what the Air Force ultimately paid. Petitioner's claim stated that, although it believed that its deduction of $4,359,000 for 1966 was the proper treatment of its loss-generating contract, it recognized that, as an alternative treatment, it might have recomputed and reduced its 1963 income (Pet. App. A44-A45). On May 13, 1968, petitioner filed a claim for refund for the taxable year 1961, based on a similar loss carryback from 1964 (*id.* at A4, A52-A53).

On November 19, 1965, approximately two years before filing the first claim for refund, petitioner filed a petition with the Tax Court for a redetermination of deficiencies for the taxable years 1961 and 1962 to account for the events described above (Pet. App. A46). On September 18, 1967, after filing the first claim for refund, petitioner amended this petition to bring before the Tax Court its taxable year 1964 "in order to allow a complete determination of [p]etitioner's Federal income tax liabilities for * * * 1961," *i.e.*, in order to claim a loss carryback to 1961 from 1964 (*ibid.*). The amendment reasserted petitioner's belief that its 1966 deduction was proper, but recognized the alternative possibility of excluding income in 1964, and thereby generating a loss to be carried back to 1961 (*id.* at A46-A48). Ultimately, the Tax Court decided the case based on the agreement and stipulation of the parties that petitioner's inclusion of the full $1,708,000 of receivables in its 1964 income was proper (Pet. App. A50-A53)—a claim that was inconsistent with the claim of a loss that could have been carried back to 1961 from 1964.

On February 28, 1972, the Internal Revenue Service notified petitioner that its 1967 deduction of $3,318,000 would be allowed, that its 1966 deduction of $4,359,000 would be

disallowed, and that its 1960 refund claim would also be disallowed because petitioner's original treatment of the anticipated income from the contact, *i.e.*, inclusion in its 1963, 1964 and 1965 returns and then deduction in 1967 in accordance with the final settlement with the Air Force, was correct (Pet. App. A58-A61).

Petitioner brought the instant suit in the Court of Claims seeking a refund of taxes for the years 1960 and 1961 for the reasons asserted in its two earlier claims for refund on the basis of net operating loss carrybacks (see pages 2-3, *supra*). The Court of Claims granted the government's motion for partial summary judgment on the ground that the claim regarding the 1961 tax year was barred by res judicata, in that the Tax Court had made a final determination of petitioner's liability for that year (Pet. App. A14-A16). The Claims Court[3] subsequently held that petitioner's 1960 claim for refund failed to satisfy Section 7422(a) of the Internal Revenue Code of 1954 (26 U.S.C.),[4] because the claim and the surrounding circumstances indicated that the claim was contingent upon the disallowance of the 1967 deduction and that deduction ultimately was allowed (Pet. App. A24-A34).

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[3]The opinion of the court was issued under the caption of the Trial Division of the Court of Claims (see Pet. App. A18). After the reorganization of the Court of Claims, final judgment was entered by the Claims Court (see *id.* at A2 n.1). Accordingly, like the court below (see *id.* at A2), we will refer to this decision as that of the Claims Court.

[4]That section provides that no suit shall be maintained for the recovery of any internal revenue tax until a claim for refund has been filed with the Secretary of the Treasury or his delegate according to the applicable regulations. Treasury Regulations on Procedure and Administration (1954 Code), Section 301.6402-2(b)(1) (26 C.F.R.), provides that a claim for refund must set forth the underlying grounds and facts sufficiently to apprise the Commissioner of the basis of the claim. See *Angelus Milling Co.* v. *Commissioner*, 325 U.S. 293 (1945); *United States* v. *Felt & Tarrant Mfg. Co.*, 283 U.S. 269 (1931).

The court of appeals affirmed (Pet. App. at A1-A13). It held that the Claims Court had correctly determined that the 1960 refund claim had not been adequately raised administratively because the claim did not apprise the Commissioner that it was anything other than a protective claim in case the 1967 deduction was disallowed (*id.* at A5-A12). The court also held that the Court of Claims' grant of summary judgment with respect to the 1961 refund claim was res judicata (*id.* at A12-A13).

2. Petitioner contends (Pet. 8-12) that the courts below erred in holding that its 1960 refund suit was barred under Section 7422(a) because its administrative claim did not adequately assert that it would still seek exclusion of the previously reported contract income on its 1963 return, even if its 1967 deduction of that same item were allowed. This contention is without merit for the reasons well stated by the court of appeals and the Claims Court (see Pet. App. A5-A12, A24-A34). The wording of petitioner's claim as an "alternative possibility" (see Pet. App. A7), the testimony of the revenue agents that petitioner characterized the claim as a protective device in case neither the 1966 nor the 1967 deductions were allowed,[5] and the ultimate allowance of the 1967 deduction, all combine to show that the Commissioner was *not* fairly apprised that the claim was operative whether or not the later deduction was allowed.

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[5]The agents testified that petitioner's tax manager repeatedly characterized both claims for refund as "protective" claims against the possibility that neither the 1966 nor the 1967 deduction would be allowed. The agents also testified that, based on this characterization and on the Internal Revenue Service's decision to allow the 1967 deduction, they did not independently verify petitioner's sales, cost of sales or inventory figures for 1963 or 1964, the years forming the basis of the refund claims, because they believed that the claims were moot by reason of the allowance of the 1967 deduction (Pet. App. A43, A54-A55, A60).

Contrary to petitioner's assertion (Pet. 10-11), this conclusion does not conflict with this Court's decision in *United States* v. *Kales*, 314 U.S. 186 (1941). In *Kales*, the taxpayer protested the assessment of taxes resulting from the government's assertion that the 1913 value of certain stock sold by the taxpayer was greater than it had ruled previously. The taxpayer argued: (1) that the assessment was illegal because the Commissioner had no authority to set aside the original valuation; and (2) that if the original valuation were set aside, she would claim a refund on the ground that the original valuation was too low. *Id.* at 196. But in direct contrast to this case, the contingency upon which the claim hinged in *Kales did* materialize; the Bureau of Internal Revenue there did set aside its original appraisal by denying the taxpayer a refund for the taxes paid pursuant to the protested assessment. Here, however, the condition precedent, *i.e.*, that the 1967 deduction would be disallowed, did not occur, and therefore the alternative claim made administratively by petitioner never materialized. Compare *National Casket Co.* v. *United States*, 16 A.F.T.R. 1001 (S.D. N.Y. 1934), aff'd per curiam, 79 F.2d 1004 (2d Cir. 1935), cert. denied, 298 U.S. 672 (1936). Moreover, the two claims presented in *Kales* were not true alternatives, in that Mrs. Kales could prevail on both counts. On the other hand, the two theories presented by petitioner here were mutually exclusive, and the claim for refund was contingent upon rejection by the IRS of petitioner's preferred theory.[6]

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[6]Petitioner's suggestion that the courts below erroneously held that the 1960 claim had been compromised (Pet. 11-12) misses the point. Neither court dismissed the 1960 claim on the ground that it had been "compromised," a term of art governed by Section 7122 of the 1954 Code and hedged with numerous formalities, including a requirement for a written agreement. Rather, the court below construed the administrative claim as being operative only if the latter deduction were disallowed. Thus, the administrative claim did not satisfy the Section 7422(a) requirement for a suit in the Claims Court once the deduction was allowed.

3. Petitioner also contends (Pet. 13-24) that its 1961 claim for refund is not barred by res judicata. Even if we assume that the court of appeals should have considered this claim even though petitioner did not seek review of the partial summary judgment order when it was entered (see Pet. 13-18; but see Pet. App. A12-A13), it is clear that the Court of Claims correctly held that petitioner's claim was barred by the Tax Court's earlier decision (see Pet. App. A14-A16). It is elementary that a determination regarding liability or non-liability relating to a particular tax year is res judicata as to any subsequent proceeding involving the same claim and the same tax year. *Commissioner* v. *Sunnen*, 333 U.S. 591, 598 (1948). Petitioner suggests that the issue it wishes to contest here is a "new" issue not resolved by the Tax Court adjudication, but that is simply not so. Petitioner had raised this precise issue—whether the anticipated contract income should be excluded in 1964 with a resulting loss to be carried back to 1961—before the Tax Court, by amendment to its petition, "in order to allow a complete determination of [p]etitioner's Federal income tax liabilities for * * * 1961 * * *" (Pet. App. A46). Petitioner informed the Tax Court, through its reply to the government's answer to the amended petition, that its original treatment of the anticipated income, *i.e.*, inclusion in 1964, was correct (Pet. App. A50). The Tax Court entered its decision regarding the 1961 year pursuant to the agreement and stipulation of the parties, and petitioner's attempt to litigate the same issue in the Court of Claims plainly was precluded by res judicata. See *Finley* v. *United States*, 612 F.2d 166, 170 (5th Cir. 1980).

Accordingly, the decision below does not conflict with the numerous cases petitioner cites regarding the res judicata effect of Tax Court decisions (see Pet. 20-25). These cases generally involved issues that had not actually been raised before the Tax Court or decided by it. See, *e.g.*,

United States v. *International Building Co.*, 345 U.S. 502 (1953). Here the issue of whether petitioner properly reported its 1964 income from the Air Force contract, the fundamental question relative to its 1961 refund claim, was actually raised in the Tax Court and there conceded by petitioner.[7]

4. Petitioner's claim (Pet. 25-27) that the decisions below deprived it of procedural due process under the Fifth Amendment because the courts did not consider all of petitioner's contentions on the merits is without foundation. Petitioner had its day in court with regard to its 1961 refund suit, where it conceded the issue that it seeks to raise again here. With regard to its 1960 refund claim, petitioner failed to file an administrative claim for refund that, under the facts and circumstances, complied with statutory and regulatory requirements. Furthermore, petitioner was allowed the claimed 1967 deduction, which, according to its refund claims and Tax Court pleadings, petitioner always believed represented the proper adjustment for its anticipated but unrealized income from the contract. In sum, petitioner's objections to the decisions below are without merit and raise no legal issue of general importance. Accordingly, review by this Court is unwarranted.

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[7]By the same token, the cases petitioner cites for the proposition that the propriety of a net operating loss carryback depends, in the first instance, on events in the loss year, not the year to which the loss is being carried back (see Pet. 21-22), are inapposite. We do not dispute the rule of the cited cases; however, the amended Tax Court petition in this case brought both the loss and the carryback years before the court, and, indeed, petitioner represented to the Tax Court that no net operating loss was warranted in 1964 by reason of the Air Force contract.

It is therefore respectfully submitted that the petition for a writ of certiorari should be denied.

REX E. LEE
Solicitor General

JULY 1983

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